Idaho Economic Forecast

DIRK KEMPTHORNE, Governor | Division of Financial Management

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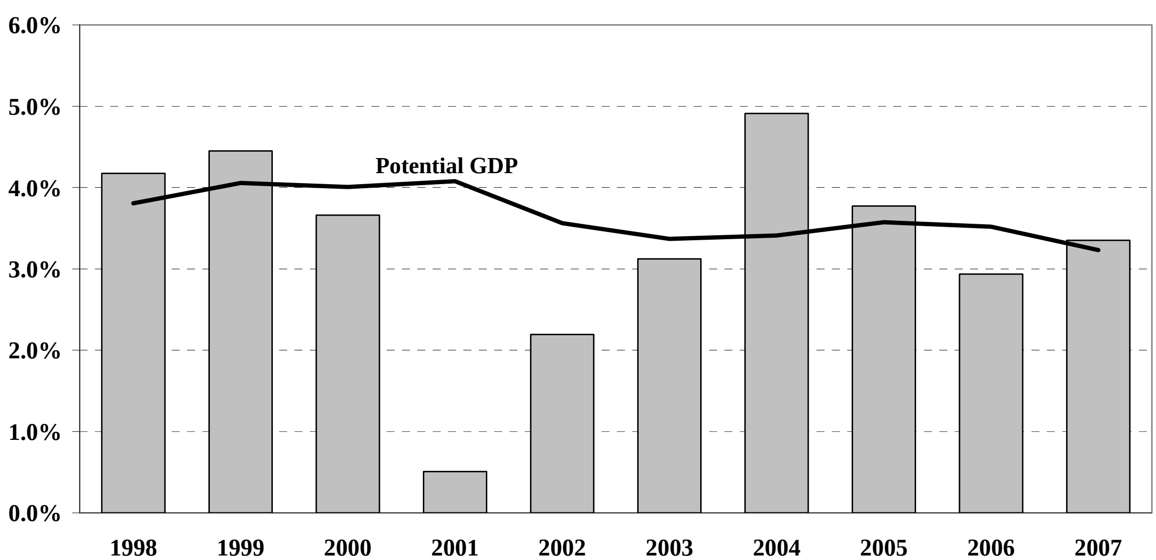
- **Forecast 2004-2007**
- **The Productivity and Jobs Connection: The Long and the Short Run of It**
- **Alternative Forecasts**

Real vs. Potential GDP Growth



Source: Global Insight

IDAHO ECONOMIC FORECAST 2004 - 2007

State of Idaho
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Governor

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PREFACE

Idaho's economy continues to grow and evolve as it enters the 21st Century. The 1980s was a decade of stop-and-start economic performance. However, it also ushered in one of the longest expansions in the state's history. Since 1987, nonfarm employment has expanded in every year and has consistently placed Idaho among the top ten fastest growing states in the nation. The 1990s saw a flood of new residents move into the state, causing the population to expand by an astounding 29% from 1990 to 2000. Over this period Idaho personal income nearly doubled. Much of the current expansion results from ongoing structural changes in Idaho's economy.

One of the biggest changes is the rise of the state's high-technology sector. Virtually nonexistent in the 1970s, this sector achieved critical mass in the 1990s to become the state's largest manufacturing employer. The growth of industry giants, such as Micron Technology and Hewlett-Packard, as well as the emergence and expansion of smaller companies, pushed payrolls above even the most optimistic forecasts made in the 1980s. The state's trade sector has also been going through a transformation. The last decade witnessed an influx of national "big box" merchandisers. During this same time, Idaho merchants successfully reached beyond the state's borders. Several regional shopping centers were established that serve locals, as well as attract shoppers from other states and Canada. Visitors fueled the surge in tourism that also benefited trade. Like its national counterpart, the service sector accounts for most of the nonfarm jobs in Idaho. Tourism has also been a boon to the service industry. While traditional factors, such as increasing discretionary income, continue to fuel the demand for services, other influences have emerged. For example, the use of temporary employees in manufacturing has bolstered business services employment. Idaho's outstanding work force has been a major factor in attracting call centers, back office operations, and credit companies.

While many changes are taking place today, traditional resource industries still play a major role in Idaho's economy. Indeed, the state's mining, agriculture, and timber sectors all experienced lulls in the late 1990s. While displaying more resilience to downturns than in the past, these industries are not totally immune from business-cycle effects. This continuing dependence on natural resources will bring a host of challenges to Idaho.

Other factors that are external to the state's economy will also present challenges to decision makers. Public policy decisions made in Washington, D.C. affect resource industry and federal installations such as the Idaho National Engineering and Environmental Laboratory and the Mountain Home Air Force Base. Finding balanced and acceptable solutions to endangered and threatened species issues and timber supply issues are of major economic significance.

In order to deal effectively with these challenges, public and private decisions need to be made with a thorough understanding of the structure of the state's economy. It is to this end that the *Idaho Economic Forecast* is directed.

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TABLE OF CONTENTS

INTRODUCTION

The national forecast presented in this publication is the June 2004 Global Insight baseline forecast of the U.S. economy. The previous *Idaho Economic Forecast* is based on the March 2004 Global Insight baseline national forecast.

The U.S. economy's recent and future performances relative to their potentials are highlighted in the cover chart. The heavy line represents the estimated potential GDP growth. This can be thought of as the economy's speed limit if it were at full employment. The bar graphs represent historical and projected GDP growth rates. The chart clearly shows that between 1999 and 2004 the economy grew much slower than its potential. It also shows this is about to change. During the four-year period encompassing 2004 to 2007, U.S. output is expected to grow faster than its theoretical ceiling. A usual consequence of real GDP breaking its speed limit is inflation. However, there appears to be enough slack capacity in the economy to prevent inflation fires from raging.

FEATURE

The United States is in the midst of a productivity boom. After slowing in the 1970s and 1980s, gains in real output per hour have soared recently. This is important because faster productivity growth leads to higher real wages and improved living standards. However, there is another view that blames strong productivity growth for the "jobless recovery." Faster productivity growth, according to this view, allows firms to increase production without increasing employment. In the article entitled "The Productivity and Jobs Connection: The Long and the Short Run of It" Carl E. Walsh illuminates the relationship productivity and jobs by distinguishing between a microeconomic and a macroeconomic perspective on productivity and between the short-run and long-run effects of changes in productivity. Dr. Walsh is a Professor at the University of California, Santa Cruz and a Visiting Scholar with the Federal Reserve Bank of San Francisco.

THE FORECAST

Alternative assumptions concerning future movements of key economic variables can lead to major variations in national and/or regional outlooks. Global Insight examines the effects of different economic scenarios, including the potential impacts of international recessions, higher inflation, and future Federal Reserve Board decisions. Alternative Idaho economic forecasts were developed under different policy and growth scenarios at the national level. These forecasts are included in this report.

Historical and forecast data for Idaho and the U.S. are presented in the tables in the middle section of this report. Detail is provided for every year from 1991 to 2007 and for every quarter from 2001 through 2007. The solution of the Idaho Economic Model (IEM) for this forecast begins with the first quarter of 2004.

Descriptions of the Global Insight U.S. Macroeconomic Model and the IEM are provided in the Appendix. Equations of the IEM and variable definitions are listed in the last pages of this publication.

CHANGES

The historical Idaho nonfarm employment data appearing in this forecast was provided by the Idaho Department of Commerce and Labor and seasonally adjusted by the Division of Financial Management. This data consists of final employment estimates through the fourth quarter of 2003 and preliminary data for the first quarter of 2004. These new historical data show the employment forecasts made in April 2004 for the fourth quarter of 2003 and first quarter of 2004 were a bit pessimistic. Specifically, actual employment was about 2,900 higher in the last quarter of 2003 than had been anticipated and was 3,115 higher than had been projected for the first quarter of 2004.

The tables in this forecast also include the U.S. Department of Commerce's Bureau of Economic Analysis (BEA) estimates of Idaho quarterly personal income through the fourth quarter of 2003. Unlike past revisions, this one was not routine. Instead, it was a major revision to the historical personal income data. The magnitude of these changes required the re-estimation of the Idaho Economic Model. The results of the re-estimation can be found in the Appendix of this *Forecast.* The BEA released its latest Idaho personal income estimates in late June 2004. These new data will be incorporated into the October 2004 *Idaho Economic Forecast*.

One change to the Idaho personal income data deserves to be highlighted. Traditionally, the BEA has provided an estimate of nonfarm personal income. However, this concept was dropped from the major revision. This is because it does not have the data necessary under the new definitions to make this estimate. In the past, BEA has calculated Idaho nonfarm personal income as Idaho personal income less farm proprietors' income, farm wages, and other farm labor income. Because of recent changes, other farm labor income is not useable, so BEA chose not to estimate Idaho nonfarm income at this time. It does intend to provide it in the future, however.

Idaho nonfarm personal income is an important measure of the state's economy, and its absence would be noticed. Because of this, DFM has estimated Idaho nonfarm income using the BEA data. Specifically, we subtracted Idaho farm proprietors' income and farm wages from total personal income. Our estimate did not consider Idaho other farm labor income, because it is not available. However, we believe its exclusion is not critical because this component is small relative to the other components. When official BEA estimates of Idaho nonfarm data become available, they will be incorporated into the *Forecast*.

The *Idaho Economic Forecast* is available on the Internet at http://www.state.id.us/dfm/econ_pub.html. Readers with any questions should contact Derek Santos at (208) 334-3900 or at dsantos@dfm.state.id.us.

SUBSCRIPTIONS

You can access the *Idaho Economic Forecast* for free at http://www.state.id.us/dfm/econ_pub.html.

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